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CHARLES ELMORE

Supreme Court of the United States

OCTOBER TERM, 1932.

No. 680

ISAAC GROSS AND JOEL GROSS, PARTNERS AS GROSS & GROSS, SOLICITORS FOR COMPLAINANT IN CHANCERY, PETITIONERS,

vs.

IRVING TRUST COMPANY, TRUSTEE CROSBY STORES, INC., BANKRUPT

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BRIEF FOR RESPONDENT.

SAMUEL KAUFMAN,
Of Counsel with Respondent.

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BRIEF FOR RESPONDENT.

(Italics ours except where otherwise noted)

Statement of Facts.

On or about the 3rd day of September, 1931, a bill was filed in the Court of Chancery of the State of New Jersey against Crosby Stores, Inc., for the appointment of a receiver for said company under Section 65 of the General Corporation Act of New Jersey, Revision of 1896. The Court appointed receivers on October 13th, 1931, who took possession of certain assets in New Jersey and continued to operate the New Jersey stores pursuant to the order of their appointment. Crosby Stores, Inc., operated a chain of five stores in New York, Massachusetts, Pennsylvania and New Jersey.

On October 14th, 1931, one day after the appointment of the State receivers, an involuntary petition in bankruptcy was filed in the United States District Court for the Southern District of New York against Crosby Stores, Inc. The Company was duly adjudged bankrupt in that District on October 30th, 1931, of which the State court receivers had notice, and on December 1st, 1931, the Irving Trust Company was elected as trustee in bankruptcy. The trustee sold the assets of the bankrupt, including those in the State of New Jersey, on December 7th, 1931.

In order to consummate the sale the United States District Court for the Southern District of New York on December 11th, 1931 by the Referee ordered the State court receivers to show cause on December 16th, 1931 why they should not turn over all the property to the trustee in bankruptcy and why they should not account to the Federal Court. This rule was made absolute on December 14th, 1931 (Record, pp. 12 and 13).

On December 14th, 1931, on notice to the trustee in bankruptcy the Court of Chancery of New Jersey made the following allowances to its receivers and counsel:

John Milton and J. S. S. Weissman, as receivers jointly	$6,000.00
Gross & Gross and William Harris, as Solicitors for the receivers, jointly, besides their taxed costs	4,000.00
Gross & Gross as Solicitors for the Complainant	350.00
	$10,350.00

On December 21st, 1931, the United States District Court for the District of New Jersey in aid of the primary

jurisdiction and pursuant to an order to show cause dated December 16th, 1931, enjoined the State Court receivers from interfering with the trustee and enjoined them from disposing of the moneys paid to them under the State Court order of December 14th, 1931 (Record, pp. 26 to 28).

The allowances were made by the Court and paid to the respective persons after bankruptcy has supervened. The trustee in bankruptcy thereupon filed a petition in the United States District Court for the District of New Jersey, alleging, among other facts, the foregoing, and asserting that the payments to the receivers were null and void and were in violation of the provisions of the Bankruptcy Act, and that it was the duty of the State Court receivers to file their accounts in the Bankruptcy Court and with their counsel appointed by the State Court to apply to the Bankruptcy Court for reasonable compensation for services rendered by them enuring to the benefit of the bankrupt estate.

The petition prayed that an order be made requiring the receivers and their counsel to turn over to the trustee in bankruptcy the assets of the bankrupt estate in their possession, including the allowances paid to them as set forth above and to file their accounts in the United States District Court (Record, pp. 1 to 41). The order was granted.

All the facts set forth in the trustee's petition were conceded below. **No objection was made to the jurisdiction of the Court or that the matter should be decided in a plenary proceeding. The parties appeared and argued the matter on the merits** (Record, p. 43).

The sole question presented is: Did the Court of Chancery of New Jersey have the power to fix the fees of its

receivers and their counsel after bankruptcy had supervened within four months of the filing of the Bill of Complaint in and the appointment of the receivers by the State Court?

History of the Conflict Between the New Jersey Court of Chancery and the United States District Court Sitting in Bankruptcy.

No statement of the issue involved here would be complete without a brief survey of the conflict that has raged in New Jersey with respect to the question as to which court should administer the affairs of a bankrupt corporation, the New Jersey Court of Chancery or the United States District Court.

New Jersey has on its statute books a corporation act* which is efficient for the winding up or re-organization of insolvent corporations. The Court of Chancery of New Jersey has been most zealous in maintaining its jurisdiction. The conflict manifested itself in

Singer v. *National Bedstead Manufacturing Co.*, 65 N. J. Eq. 290 (1903),

an opinion by Stevenson, V. C., who said at page 299:

> "As the Bankruptcy Act stood until the recent amendments I am unable to perceive how, when the Court of Chancery has acted under the New Jersey Statute relating to insolvent corporations * * * and has then as a necessary result appointed a receiver of the corporate assets; a receiver subse-

* See Appendix A.

quently appointed by a bankrupt court—*i. e.*, appointed subsequent to the vesting of the assets in the Chancery receiver under our statute or a trustee appointed under a subsequent adjudication of bankruptcy—can acquire title to those assets.

The title which the trustee in bankruptcy takes is defined in the Bankrupt Act and practically includes only the property which belonged to the bankrupt at the time of the adjudication and property theretofore transferred by him by way of preference or in fraud of creditors."

And at page 307 he said:

"Therefore the order of this Court will direct that the receiver of this Court present his account and report, that proper allowances to the two receivers of this Court be paid and that the residue of the assets be turned over to the bankruptcy receiver, and that the receiver appointed by this Court be thereupon discharged from his office."

From this practice inaugurated in 1903 there was no deviation until the present time and the Federal Court in New Jersey tolerated this procedure until the cases of

Isaacs v. *Hobbs Tie & Timber Co.*, 282 U. S. 734

was decided by this Court, with the resultant opinion in

Silberberg v. *Ray Chain Stores, Inc.*, 54 Fed. (2) 650 (D. Ct.), 58 Fed. (2) 766 (Circuit Court). Certiorari denied by this Court, *Sub nomine;*

Winne & Casey v. *Silberberg*, 77 L. Ed. 35, Vol. I, Adv. Rep. 1932 Term, page 35.

After the *Singer* case, *supra,* there was an interval of peace until

> *Cavagnaro* v. *Indian Tire & Rubber Co.,* 90 N. J. Eq. 532 (1919) and
> *Cudahy* v. *N. J. Dairy Products Co.,* 90 N. J. Eq. 541 (1919)

were decided, both opinions being by Lane, V. C.

In the *Indian Tire & Rubber Co.* case (*supra*), directors of a New Jersey corporation were held guilty of contempt of court for filing a petition in bankruptcy after the New Jersey Court had appointed Chancery receivers and had restrained the company, its officers, directors and agents from exercising the privileges and franchises granted by the State of New Jersey. The decision can be justified on the ground that the directors and officers prior to the filing of the petition in bankruptcy had removed property from the possession of the State Court receiver.

In the *Cudahy* case (*supra*), the Court laid down the rule that State Court receivers after bankruptcy has supervened, *must* first account to the State Court, receive their compensation from the State Court and then turn the balance over to the trustee in bankruptcy. The Court held:

> "The receiver may not, without the consent of this Court, either submit to the jurisdiction of the bankruptcy court to fix his compensation, or turn over to the trustee in bankruptcy, or to any other officer of the bankruptcy court, or of any court, any of the assets within his control."

This case was a logical extension of the rule laid down in *Singer* v. *National Bedstead Manufacturing Co.* (*supra*).

During this period the State Courts carried the battle directly to the Federal Court without any let up in their drive. Every type of order decree or injunction which could in any way hamstring the Federal Court and prevent creditors and the corporation from applying for relief to the Federal Courts was availed of in the State Court. The terrible weapon of contempt was threatened and used. The State Court, among other things, enjoined:

> (a) Creditors from instituting, prosecuting or continuing the prosecution of any action instituted under and by virtue of the United States Bankruptcy Court without first giving notice to the equity receiver.[1]
>
> (b) The corporation, its officers, servants and agents from taking any corporate action for the purpose of having a receiver appointed in any other cause.[2]
>
> (c) Stockholders and all other persons from instituting, prosecuting or proceeding with any action in any court—at law or in bankruptcy.[3]

In one case[4] the State Court directed its receiver not only to retain in his possession all of the assets but not to surrender the assets to a trustee in bankruptcy until he had accounted to and received his compensation from the State Court.

The Court recently issued orders in at least two cases[5] directing officers, directors and creditors to show

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[1] See Appendix B.
[2] See Appendix B.
[3] See Appendix B.
[4] See Appendix B.
[5] See Appendix B.

cause why they should not be punished for contempt for filing petitions in bankruptcy after the State Court had appointed equity receivers.

It is manifest therefore that the struggle has been sharp and bitter. Recently the conflict dwindled down to the question presented in the case at bar, which Court has the power to fix fees? It would appear, except for sporadic injunction orders, that the State Court has yielded on every other point relating to the paramount jurisdiction of the Federal Court sitting in bankruptcy, namely, that creditors may file involuntary petitions; that the corporation may file a voluntary petition or consent to be adjudicated in involuntary proceedings, notwithstanding the fact that the State Court had appointed a State receiver. They still vigorously maintain, however, that the right to fix fees is inherent in their Court.

When this Court decided *Isaacs* v. *Hobbs Tie & Timber Co.* (*supra*), the United States District Court for the District of New Jersey through Judge Fake critically re-examined the practise that had prevailed in New Jersey for about thirty years and came to the conclusion that it was in violation of the Bankruptcy Act of the United States. The first case that came before him was

Silberberg v. *Ray Chain Stores, Inc.* (*supra*).

In that case Judge Fake *himself had appointed Federal equity receivers* in the United States District Court for the District of New Jersey. Bankruptcy supervened and he held that he was without power to fix the fees and that the application would have to be made in the Bankruptcy Court. That case was affirmed by the Circuit Court of Appeals for

the Third Circuit and certiorari was denied by this Court (*supra*).

In the answer to the petition for the writ of certiorari in the Ray Chain case mention was made of the fact that the case at bar was en route to this Court and it was hoped that the Court would review both orders to the end that a final opinion would be rendered which would definitely terminate the unseemly controversy between courts of independent sovereignties. A survey of the conflict may be found in

The current conflict between the Court of Chancery and the Bankruptcy Court (1932) 1 Mercer Beasley Law Review, pages 3 to 19.

Note (1932) 41 Yale L. J. 1234-1237.

After this Court refused to review the Ray Chain case the Court of Chancery promptly held it was only applicable to a Federal Court sitting in equity and that it did not and could not apply to a State Court. They stated in effect they would not follow it until this Court spoke authoritatively on the subject and doubted the power of the Court so to speak. The latest expression by the State Court in this field of troublesome jurisdiction is

Isenberg v. *Kimberley Phonograph Co. of New Jersey*, 111 N. J. Eq. 195 (1932).

The Court held at page 198:

> "The trustees in bankruptcy appear by their solicitors, and object not only to the making of the order for allowances in the amount and in the form asked by the receiver, but to the making of any

allowances whatever by this court; their contention being that this court is without power to make such allowances under the authority of Isaacs *v.* Hobbs Tie & Timber Co., 282 U. S. 734; Silberberg *v.* Ray Chain Stores, Inc., 54 Fed. Rep. (2) 650, aff'd 58 Fed. Rep. (2d) 766; Moore *v.* Scott, 55 Fed. Rep. (2d) 863; Lion Bonding & Surety Co. *v.* Karatz, 262 U. S. 640, and Bloch *v.* Bloch, 86 N. Y. Supp. 1047.

"The proposition that this Court, after an adjudication of bankruptcy, is without jurisdiction or power to fix the compensation of its receiver duly appointed on adjudication of insolvency prior to any bankruptcy proceedings, is one *in which this court cannot concur and to which it cannot yield unless upon explicit and controlling authority.* In the view of this court, the federal legislation does not purport expressedly or impliedly, to effect any such result; *and even if it did, the constitutional validity of such an attempt would be, to say the least, open to serious question.*

"Of the decisions mentioned above, the first is by no means an explicit authority for the proposition of the trustee; the next two are not in point, for they involve federal equity receivers instead of receivers of state courts; the expression in the fourth is dictum; and the last is in nowise controlling upon this court."

POINTS UPON WHICH THE RESPONDENT RELIES.

The propositions for which the respondent respectfully contends, and upon which it relies, are the following:

I.

The case at bar does not involve the question of jurisdiction by summary process or plenary proceeding.

II.

The jurisdiction of the United States District Court in Bankruptcy is paramount.

III.

The State Court is without power to fix the fees of its officers, bankruptcy having supervened within the four months' period.

IV.

The power to fix fees after bankruptcy supervenes is exclusively in the Bankruptcy Court.

V.

A State Court receiver is entitled to and will receive from the Bankruptcy Court just compensation and the repayment of his expenses for benefiting or preserving the bankrupt estate.

ARGUMENT.

POINT I.

The case at bar does not involve the question of jurisdiction by summary process or plenary proceeding.

The first specification of error in the petition for writ of certiorari (p. 13 of Petition) sets up that the United States Circuit Court of Appeals erred in holding that it had jurisdiction in bankruptcy in a summary proceeding to direct the state court receivers and their counsel to turn over to the trustees in bankruptcy the fees which had been paid them after the petition in bankruptcy had been filed.

It is well, therefore, at this time to give the background of the litigation. The trustee filed his petition as it is set forth in the Record (pages 1 to 41). The respondents filed a special appearance with the Clerk of the United States District Court objecting to the jurisdiction of the Court to hear the matter in a summary way. The respondents then withdrew their special appearance and submitted to the jurisdiction. They filed no answer to the petition of the trustee and conceded that the facts stated in the petition were correct and argued the matter on the merits (Record, p. 43). The Court held that the issue was squarely within *Silberberg* v. *Ray Chain Stores, supra,* and decided in favor of the trustee (Record, p. 43). The order granting the prayers of the petition is set forth in full in the Record (pages 44 and 45), and recites "that the matter came on regularly to be heard in the presence of" counsel (Record, p. 45). No objection to the jurisdiction was made or argued

before Judge Fake sitting below. No objection was made in the Circuit Court of Appeals on the argument on the appeal of the order and the matter was neither argued nor briefed by respective counsel.

The first time the objection appears is in the petition for the writ of certiorari to this Court. The reason for the assignment of error is due to some superfluous language by Judge Thompson in the Circuit Court of Appeals. In the opinion of the Circuit Court of Appeals, Judge Thompson said:

> "The State receivers contend that recovery of the compensation and fees already allowed could be had only in a plenary suit and that the District Court had no jurisdiction in a summary proceeding to order them to account to the trustee."

We are at a loss to understand how the Court arrived at the conclusion that the appellants in the Court below, the petitioners here, made such a contention. It was not made orally at the argument before the Court; it does not appear anywhere in the record below; it does not appear in the briefs below. We, therefore, submit that an objection to the jurisdiction consented to below cannot be urged on writ of certiorari in this Court.

An objection to the jurisdiction to hear a matter in a summary way may be waived. The jurisdiction may be conferred on the Bankruptcy Court by consent.

> *Bardes* v. *First National Bank of Hawarden*, 178 U. S. 524, at 539, 44 L. ed. at page 1175.

See also

> *MacDonald* v. *Plymouth County Trust Co.*, 42 Sup. Ct. 505; 76 Law ed., page 1093; 286 U. S. 263,

where the Court held that a referee may, if the parties consent, try the issues which must otherwise be tried in a plenary suit brought by the trustee. It follows therefore if the jurisdiction may be conferred on the referee it most certainly can be conferred on the Court itself. See also

Page v. *Arkansas Natural Gas Corp.*, 52 S. Ct. 5071; 76 L. ed., page 1096; 286 U. S., page 269.

The facts in this case are squarely within

Clark v. *Larremore*, 188 U. S. 486, 47 L. ed. 555; 23 Sup. Ct. Rep. 363,

set up in footnote 25 to *Taubel-Scott-Kitzmiller Co.* v. *Fox*, 264 U. S. 425, 66 L. ed. 770, 44 S. Ct. 396, where it is pointed out that the objection to the jurisdiction was first raised but later withdrawn.

We therefore submit that the objection to the jurisdiction having been waived below it cannot be raised anew in this Court.

Assuming that it has been properly raised, the contention of the petitioners is conclusively determined by the opinion of this Court in

May v. *Henderson*, 268 U. S. 111.

> "In consequence, any person acquiring an interest in property of the bankrupt or his assignees for the benefit of creditors, adverse to the creditors, after the filing of a petition, with notice of it, may be directed to surrender the property thus acquired by summary order of the bankruptcy court. Re Denson, 195 Fed. 854; Re Rudnick, 158 Fed. 223; and see White *v.* Schloerb, *supra.*"

* * * * * *

> "We rest our decision rather on the duty of assignees for the benefit of creditors to account in a summary proceeding for the property which they have received within four months of the bankruptcy, and to make restitution of the value of the property of the bankrupt which they have dissipated without a colorable claim of right."

See also *Re Diamond Estate*, 259 Fed. 70 (C. C. A., 6th), 1919.

POINT II.

The jurisdiction of the United States District Court in Bankruptcy is paramount.

It is rather remarkable that at this stage of our Federal Jurisprudence it becomes necessary to cite cases relating to the paramount jurisdiction. The Constitution of the United States provides that:

Section 8, sub-division 4:

> "The Congress shall have power to establish * * * uniform laws on the subject of bankruptcies throughout the United States."

Congress has enacted various Bankruptcy Acts, the most recent of which is the Bankruptcy Act of 1898, Section 9, U. S. Comp. Statutes (1910), page 11,007, and that Act creates the United States District Courts as bankruptcy courts. The Act provides that

> "Courts of Bankruptcy shall include the District Courts of the United States and of the Territories * * * Bankruptcy Act of 1898, Section 1, sub-division (8)."

The purpose of the Constitutional provision hereinabove referred to was discussed only casually in *The Federalist No. XLII*, page 292, because its necessity was so apparent. James Madison wrote as follows:

> "The power of establishing uniform laws of bankruptcy is so intimately connected with the regulation of commerce, and will prevent so many frauds where the parties or their property may lie or be removed into different states, that the expediency of it seems not likely to be drawn into question."

In *Isaacs* v. *Hobbs, supra*, this Court said:

> "The jurisdiction in bankruptcy is made exclusive in the interest of the due administration of the estate and the preservation of the rights of both secured and unsecured creditors."
>
> • • • • • •
>
> *"Indeed a Court of Bankruptcy itself is powerless to surrender its control of the administration of the estate."*

This was merely a restatement of the law as found in the host of earlier cases.

Sturges v. *Crowninshield*, 4 Wheat. 122;
Mueller v. *Nugent*, 184 U. S. 1;
Watts & Sachs, 190 U. S. 1;
International Shoe Co. v. *Pinkus*, 278 U. S. 261;
U. S. F. & G. Co. v. *Bray*, 225 U. S. 205;
Lion Bonding & Surety Co. v. *Karatz*, 262 U. S. 640;
Larazus v. *Prentice*, 234 U. S. 263.

These representative cases have imbedded in our law the doctrine that in the administration of the assets of a bankrupt the Federal Court sitting in bankruptcy is paramount and once bankruptcy has supervened within the four months' period, all courts, whether State Courts or Federal Equity, are prohibited from interfering with the administration of the affairs of a bankrupt. This disposes of the statement set forth on page 6 of petitioners' brief that "the receiver in bankruptcy and the trustee in bankruptcy acquiesced in the conduct of the business located in New Jersey by the receivers in Chancery." A bankruptcy court cannot surrender the administration of its trust imposed upon it by the Constitution and the Bankruptcy Act of the United States as was clearly set forth in *United States Fidelity & Guaranty Company* v. *M. J. Bray* and *Isaacs* v. *Hobbs Tie & Timber Co., supra.* It would have been futile in the light of the conflict between the State Court and the Federal Court sitting in bankruptcy to have appointed a receiver in bankruptcy and attempted to wrest this property out of the possession of the State Court receiver in view of the orders then being entered in the Court of Chancery of the State of New Jersey directing its receivers not to surrender assets to receivers or trustees in bankruptcy, but to hold them adversely to said receivers and trustees (see Appendix B). It is because of this conflict and this refusal by the State Court that this case is now being presented for final disposition.

The New Jersey Court of Chancery insists that although the states ceded this power to the Federal Government when the Constitution was adopted it nevertheless retained a scintilla of jurisdiction to fix the fees of State Court receivers appointed under the State Corporation Act.

POINT III.

The State Court is without power to fix the fees of its officers, bankruptcy having supervened within the four months' period.

Isaacs v. *Hobbs, supra,* at once focussed the attention of bench and bar on the Constitutional provisions hereinabove referred to, which had been ignored, overlooked or misunderstood for some time. In

Mueller v. *Nugent,* 184 U. S. 1,

this Court said that:

> "The filing of the petition is a caveat to all the world, and in fact an attachment and an injunction."

The doctrine of this case was vigorously reasserted in

May v. *Henderson,* 268 U. S. 111,

where the Court held in addition:

> "that the Courts of Bankruptcy do not permit themselves to be ousted of jurisdiction by the mere assertion of an adverse claim."

In

Straton v. *New,* 283 U. S. 318,

the Court again held that upon the filing of a petition in bankruptcy the

> "proceeding is so far *in rem* that the estate is regarded in *custodia legis* from the filing of the petition."

* * * * * *

> "It follows that liens cannot thereafter be obtained *nor proceedings be had in other courts to reach the property,* the District Court having acquired the exclusive right to administer all property in the bankrupt's possession" (citing cases).

See also *Taubel-Scott Kitzmiller Co.* v. *Fox,* 264 U. S. 425.

Yet despite these clear-cut unmistakable declarations by this Court the New Jersey Court of Chancery still asserts it alone may and should fix the fees of its receivers even after the filing of a petition in bankruptcy which is, as the Federal Courts say, THE ASSERTION OF THE PARAMOUNT JURISDICTION.

An examination of the cases reveals that they fall in four groups.

Group I.

Appointment of a State Court receiver and within four months thereafter a petition in bankruptcy is filed against the insolvent corporation. The State Court receiver then transfers *all* of the assets to the bankruptcy receiver or trustee. May the State Court then fix the fees of its appointee?

Even the New Jersey Court of Chancery concedes that in this type of case it will not fix the allowance of its receiver. In

> *Cudahy* v. *N. J. Products Co.,* 90 N. J. Eq., 541 (*supra*),

the Court, by Lane, V. C., said:

> "In such cases, however desirous the individual members of the Court may be to lend any aid or as-

> sistance possible to the Federal Courts, the Court will not ordinarily fix the compensation or indicate officially its views as to the proper amount. The Court will not ordinarily make an order or decree which cannot be made effective by its own process."

Cases in Group I present no difficulty whatsoever. They solve themselves. The assets having been surrendered the State Court is powerless to fix and pay the fees.

Group II.

Appointment of a State Court receiver and the conversion by him of all of the assets into cash, the passing of his account, the fixing of his fees *and the payment thereof prior to the filing of the petition in bankruptcy within the four months' period.*

The rule governing this case falls within:

> *Louisville Trust Co.* v. *Comingor,* 184 U. S. 18 (generally known as the Comingor case);
> *Galbraith* v. *Vallely,* 256 U. S. 46;
> *May* v. *Henderson, supra.*

Much stress may be laid upon the *Comingor case, supra,* but we submit that the petitioners can gain nothing therefrom. The facts in that case were as follows:

The assignee had disbursed moneys and had paid to himself his assignee's fees PRIOR TO THE FILING OF THE PETITION IN BANKRUPTCY. The referee directed him to turn the fund over as a result of a summary proceeding commenced against him in the bankruptcy court. The assignee *filed an objection to the jurisdiction of the Court by summary proceedings asserting he was an adverse claimant.*

This Court held that since he had expended the moneys *prior to the filing of the petition in bankruptcy,* he was in the position of a *bona fide* adverse claimant and the moneys so adversely held could not be reached by the summary process of the bankruptcy court. He was entitled to the benefits of a plenary suit.

No such facts are presented in the case at bar. There was no objection to the jurisdiction of the Court. The respondents had waived it by withdrawing their special appearance. Second, the fees in this case were paid *after* the petition in bankruptcy had been filed, since it is a fact that the bankruptcy petition was filed one day after the appointment of the State Court receivers.

In *Galbraith* v. *Vallely* (*supra*) the facts were precisely the same as in the Comingor case and the decision reaffirmed the doctrine that the procedure was to be by summary process.

The doctrine of the Comingor case was reaffirmed in *May* v. *Henderson* (*supra*), but the Court justified summary procedure since the payments in the May case were made after the filing of the petition in bankruptcy.

The Comingor, Galbraith and May cases all dealt with assignees. However, the doctrine with respect to assignees has been extended to receivers.

Stellwagen v. *Clum,* 245 U. S. 606.

Group III.

Appointment of a State Court receiver, the conversion by him into cash of all the assets and the filing of a petition in bankruptcy within four months and *before* his

accounts have been approved and his fees fixed and paid by the State Court.

Group IV.

Appointment of a State Court receiver and the filing of a petition in bankruptcy within four months and *before* the State Court receiver has converted the assets into cash.

The cases within Groups III and IV present the difficult ones for the Courts. While some Courts treat Groups III and IV separately, they will be considered as one here, for, it is submitted, an analysis of the cases indicates there is no difference in principle between the two problems.

One of the most recent cases in New Jersey is

> *Colton* v. *Bankshares Corp. of the U. S.*, 108 N. J. Eq. 417, 155 Atl., p. 471,

wherein the Court said:

> "The practise as laid down in Schachat *v.* Standard Auto Supply Co., 106 N. J. Eq. 105, 150 Atl. 183, is that indicated in *Re* Watts & Sachs, 190 U. S. 1, 23 S. Ct. 718, 47 L. ed. 933, which has ever since been the guide of Courts and lawyers in this State, that the Court of primary jurisdiction may supervise the administration of its receivers and fix their compensation, and it will be adhered to."

In

> *Schachat* v. *Standard Auto Supply Co.*, 106 N. J. Eq. 105 at 110,

the Court dismissed the language of Mr. Justice Brandeis in *Lion Bonding & Surety Co.* v. *Karatz*, 262 U. S. 64 (*supra*), as follows, Mr. Justice Brandeis speaking for the Court said:

> "Even where the Court which appoints a receiver had jurisdiction at the time but loses it, as upon supervening bankruptcy, the first court cannot thereafter make an allowance for his expenses and compensation. He must apply to the bankruptcy court."

Vice-Chancellor Church said in the Schachat case, *supra:*

> "The remarks of Mr. Justice Brandeis were purely *obiter.*"

Since every case in the State of New Jersey relies upon

Re Watts & Sachs, 190 U. S. 1,

it is necessary critically to re-examine that case to see whether it justifies the conclusions which the New Jersey Court has so vigorously asserted.

A State Court receiver had turned over the property to the bankruptcy receiver. Thereafter, on the advice of their attorneys, the State Court receiver, through a Sheriff, forcibly seized the property and took it from the possession of the bankruptcy receiver. The sole question in the case, therefore, was whether the attorneys who had given their advice in good faith and in the discharge of their duty as counsel could be deemed guilty of contempt of the bankruptcy court and punished as contemnors.

The Court held the attorneys could not be adjudged guilty of contempt of court, but during the course of its opinion made certain statements which the State Courts seized and relied upon for their decisions. The first statement is as follows:

> "The general rule as between courts of concurrent jurisdiction is that property already in possession of the receiver of one court cannot rightfully be

> taken from him without the court's consent, by the receiver of another court appointed in a subsequent suit; but that rule can have only a qualified application where winding up proceedings are superseded by those in bankruptcy as to which the jurisdiction is not concurrent. Still it obtains as a rule of comity, and accordingly the receiver of the district court brought his appointment to the knowledge of the Floyd Circuit Court and requested the delivery of the assets."

It may be argued that in this language the Court meant to say that the general rule, which applies between courts of concurrent jurisdiction while not strictly applicable as between courts of paramount and subordinate jurisdiction, does nevertheless obtain as a "rule of comity," and if the words "rule of comity" are understood to mean a binding and controlling rule of law, a plausible support is thus found for the view that in fact the Federal Bankruptcy Court *should* adopt the same rule which the Federal Court sitting in Equity applies where it merely has concurrent jurisdiction with the State Courts.

The complete answer to this argument however, is that the words "rule of comity" as used by Chief Justice Fuller means no more than a "rule of etiquette" rather than a "rule of law". The word "comity" is defined in *11 Corpus Juris, page 1235,* as follows:

> "*Comity.* Generally, complaisance, concession, courtesy, courtesy between equals, friendly civility, respect, reciprocity, a disposition to accommodate, good will, the granting of a privilege, *not of right* but of good will, a willingness to grant a privilege, *not as a matter of right,* but out of deference and good will."

In

The Paquette Habana, 175 U. S. 677, 44 L. ed. 320 at page 326,

the Court, referring to an opinion in the English case of *The Young Jacob and Johanna*, 1 C. Rob. 20, says:

> "The opinion begins by admitting the known custom in former wars not to capture such vessels; adding, however, 'but this was a rule of comity only, and not of legal decision.'
>
> * * * * * * *
>
> "The word *comity* was apparently used by Lord Stowell as *synonymous with courtesy or good will.*"

The same view of the meaning of the word "comity" was expressed by this Court in

Wilcox v. *Consolidated Gas Co.*, 212 U. S. 19, 53 L. ed. 382,

where the Court said by Mr. Justice Peckham:

> "At the outset it seems to us proper to notice the views regarding the action of the Court below, which have been stated by counsel for the appellants, the public service commission in their brief in this court. They assume to criticize the court for taking jurisdiction of this case, as precipitate, as if it were a question of *discretion* or *comity*, whether or not that court should have heard the case. *On the contrary there was no discretion or comity about it.* When a Federal Court is properly appealed to in a case over which it has by law jurisdiction, it is its duty to take such jurisdiction."

The true nature of the so-called "comity doctrine" appears fully when the real rule is recognized that it

applies only between courts of *concurrent* jurisdiction and does not apply as between courts of paramount and subordinate jurisdiction. This was enunciated by this Court in

Covell v. *Heyman* 111 U. S. 176, 28 L. ed. 391,

where the Court said:

> "A principle", he said, 'which is essential to the dignity and just authority of every court and to the *comity* which should regulate the relations between *all* courts of concurrent jurisdiction;' 'that principal is,' he continued, 'that whenever property has been seized by an officer of the court, by virtue of its process, the property is to be considered as in the custody of the court, and under its control for the time being; and that no other court has a right to interfere with that possession *unless it be some court which may have* a direct supervisory control over the court whose process has first taken possession, or *some superior jurisdiction* in the premises."

It is this doctrine that fundamentally underlies *U. S. F. & G. Co.* v. *Bray,* 225 U. S. 205, where the Supreme Court laid down the rule that a Court of Bankruptcy:

> "was not at liberty to surrender its exclusive control over matters of administration, or to confide them to another tribunal."

See also

Harkin v. *Brundage,* 276 U. S. 36;
Welch v. *O'Neill,* 245 Fed. 261 (C. C. A. 3rd);
People v. *N. Y. City Rwy. Co.,* 107 N. Y. Supp. 247.

Chief Justice Fuller recognized this doctrine that the bankruptcy court's jurisdiction is exclusive, for he said in the *Watts* case:

> "The bankruptcy law is paramount, and the jurisdiction of the Federal Courts in bankruptcy, when properly invoked, in the administration of the affairs of insolvent persons and corporations, is essentially exclusive."

It is therefore apparent that Chief Justice Fuller merely used the words "rule of comity" in this case in the sense of "courteous," for he said, and

> "accordingly the receiver of the District Court (Federal Court) brought his appointment to the knowledge of the Floyd Circuit Court and requested the delivery of the assets."

But Vice-Chancellor Backes in *Colton* v. *Bankshares Corp. of U. S.* (*supra*), used the word "comity" as a controlling rule of decision, viz.:—"*Comity which obtains as between courts of concurrent jurisdiction.*" In support of his views as to the "comity rule" he cites

> *Wabash R. R. Co.* v. *Adelbert College*, 208 U. S. 38, 52 L. Ed. 379,

which case however merely involved *concurrent* jurisdiction between Federal and State Courts and not a question of paramount versus inferior jurisdiction as is presented in the case at bar.

The second statement made by the Supreme Court in the *Watts* case (*supra*) and which language is the veritable bulwark of the Court of Chancery opinions is as follows:

> "It has been already assumed that the bankruptcy proceedings operated to suspend the further administration of the insolvents' estate in the State Court, but it remained for the *State Court to transfer the assets,* settle the accounts of its receiver and close its connection with the matter. Errors, if any, committed in so doing could be rectified in due course and in the designated way."

The State Courts have undertaken to determine that the words "settle the accounts" means also "and fix the allowances for the receiver." If the order of the words means anything, the duty of the state receiver is to transfer the assets first. In

> *Bouvier's Law Dictionary,* page 107 (Third Revision being Eighth Edition),

this definition of "settling the account" is given:

> "A statement of the receipts and payments of an executor, administrator or other trustee of the estate confided to him."

See also 53 *Corpus Juris,* pp. 368, *et seq.* and pp. 381, *et seq.,* where it will be found that the matter of accounting by receivers and the settlement of receivers' accounts are treated as a wholly separate and distinct matter from the treatment of allowances to receivers. It is possible that a court might settle the accounts—that is, approve the receipts and disbursements and yet not award compensation.

In *Silberberg* v. *Ray Chain Stores* (*supra*), Judge Fake with patient research traced the further developments of the Watts case and disclosed that the State officers sought their allowances not from the State Court, but from the Federal Court and compensation was denied them because

compensation could only be awarded them for services rendered in benefitting and conserving the estate.

See

Re Zier & Co., 127 Fed. 399 affirmed in 142 Fed. 102 (C. C. A. 7th).

If the language of Chief Justice Fuller had the meaning as set forth in *Colton* v. *Bankshares Corporation, supra*, the officers in *Re* Zier would have applied to their State Court. Of course had they rendered services which enured to the benefit of the estate, the Federal Court would have awarded them reasonable compensation under *Randolph* v. *Scruggs*, 190 U. S. 533.

In

Bloch v. *Bloch*, 86 N. Y. Supp. 1047

Mr. Justice Clark of the New York Supreme Court dealt with the precise question as in the case at bar within the scope of the cases falling in Groups III and IV, *supra* (pp. 21 and 22). The question in the Bloch case was whether the Court could make allowances to its own receiver after bankruptcy had intervened. The Court held at page 1050 in speaking of Mr. Justice Fuller's remark about "settling the accounts":

> "In view of the main purpose of the bankruptcy law, and the decisions rendered, I am of the opinion that the settlement of the accounts mentioned *does not mean the disbursement by the State Court of assets unadministered* at the time the proceedings in bankruptcy have been brought, a receiver thereunder appointed, and a demand for the property made. This Court may, upon motion duly made, settle the

> accounts of its receiver, recognizing such payments as were already properly made before the petition in bankruptcy was filed (Louisville Trust Co. *v.* Comingor, 184 U. S. 18) and upon transfer of all assets in possession to the bankruptcy court close his account, cancel his bond and discharge him and his sureties' from liability. The motion of the receiver in bankruptcy that the receiver in this suit (the State action) pay over the $10,000.00 in question to the receiver in bankruptcy is granted but without costs. Settle order on notice. Upon such payment the receiver in this suit may apply to this court for a settlement of his accounts and for his discharge."

It is submitted that the Court in the Bloch case clearly recognized that the bankruptcy jurisdiction was paramount and correctly applied the principle of the Watts case as was intended by this Court, both in the Watts case and in *Lion Bonding & Surety Co.* v. *Karalz, supra.*

POINT IV.

The power to fix fees after bankruptcy supervenes is exclusively in the Bankruptcy Court.

The best case on this subject and which reviews all of the cases on the subject is

Re Diamond Estate, 259 Fed. 70 (C. C. A., 6th).

The Court held:

> "Assuming that the action of the state court in respect to allowances to its receiver was presumptively correct and just, and that the bankruptcy court

will give due weight to this presumption, yet the ultimate determination of that question must, under the facts of this case, rest with the court of bankruptcy, taking into account equitable considerations and the extent to which the bankrupt estate has been benefited by the services and disbursements of the state court receiver. In re Watts & Sachs, *supra;* In re Zier & Co. (C. C. A., 7th), 142 Fed. 102, 103, 73 C. C. A., 326; Hume *v.* Myers (C. C. A., 4th), 242 Fed. 827, 830, 831, 155 C. C. A., 415; In re Neuberger (C. C. A., 2nd), 240 Fed. 947, 153 C. C. A., 633. Any other rule would, *pro tanto,* take the ultimate distribution of the assets of the bankrupt estate out of the hands of the bankruptcy court. We have no occasion to consider what the effect would have been had the state court fixed its receiver's compensation and allowances for merely the 18 days prior to bankruptcy. No action thus limited was had or asked and the superior court, as the court of appointment, has since surrendered any claim of control over the subject. As the case stands, orderly administration will be best effected by treating the entire period of service as a unit."

* * * * * *

"The pendency of proceedings in the state appellate court for review of the state court's action of November 21st, setting aside its previous order for compensation, is not and could not well be urged against the jurisdiction of the bankruptcy court. The commendable action of the state court last referred to terminated any conflict between the federal and state courts. The legality of that order and of its predecessors, as affecting the jurisdiction of the bankruptcy court, is one arising under the bankruptcy law, which it is our duty to decide."

This Court refused to grant a writ of certiorari *sub-nomine.*

Frankenstein v. *Jacobs,* 249 U. S. 614; 63 L. ed. 802.

This case established the following rules of law:

(a) *That the bankruptcy court is the only court that can fix fees after bankruptcy has supervened.*

(b) That summary proceedings are proper to recover moneys paid to state court receivers *after bankruptcy has supervened.*

This case was cited with approval in

May v. *Henderson,* 268 U. S. 111.

In this case assignees made payments before and after bankruptcy had supervened to a bank on account of an indebtedness due from the assignor to the bank. One of the assignees was the president of the bank. After bankruptcy supervened the referee made an order that the assignees account and turn over the moneys to the trustee in bankruptcy.

A similar procedure was adopted in the case at bar. The respondents were ordered to account and turn over the moneys they should have had but for the payments they made to themselves after bankruptcy had supervened.

In the case at bar the record indicates the receivers knew of the bankruptcy proceedings. As a matter of fact bankruptcy followed immediately on the heels of their appointment. No objection was made to the procedure. The respondents appeared and argued the merits. The language of Mr. Justice Stone, speaking for the Supreme Court, is therefore applicable.

"But property held or acquired by others for account of the bankrupt is subject to a summary order of the court, which may direct an accounting and a payment over to the trustee or receiver appointed by the bankruptcy court (citing cases)."

* * * * * *

"Such is the rule with respect to assignees for the benefit of creditors within four months of the filing of the petition (citing cases among them *Re Diamond, supra*)."

* * * * * *

"The several amounts debited to the account, with the assent or connivance of the assignee *subsequent* to the filing of the petition, fall clearly within the rule that, as to property in the hands of the bankrupt, or held by others for his account, 'the filing of the petition is a caveat to all the world and in fact an attachment and an injunction' * * * (citing cases). In consequence, any person acquiring an interest in property of the bankrupt or his assignee for the benefit of creditors, adverse to the creditors, *after* the filing of a petition, with notice of it, may be directed to surrender the property thus acquired by summary order of the bankruptcy court."

* * * * * *

"While it is now settled that the claim of an assignee for the benefit of creditors, of the right to charge in his account expenses incurred or expenditures made *prior* to the filing of the petition in bankruptcy, is an adverse claim which cannot be adjudicated in a summary proceeding (Louisville Trust Co. *v.* Comingor, 184 U. S. 18, 46 L. ed. 413, 22 Sup. Ct. 293, Galbraith *v.* Vallely, 256 U. S. 46, 65 L. ed. 823, 41 Sup. Ct. Rep. 415), we think the rule cannot be extended to a case such as this, where the claim is

merely colorable, and on its face made in bad faith and without any legal justification."

* * * * * *

"We rest our decision rather on the duty of assignees for the benefit of creditors to account in a summary proceeding for the property which they have received within four months of the bankruptcy, and to make restitution of the value of the property of the bankrupt which they have dissipated without a colorable claim of right."

We submit that this case fixes the rights of the petitioners. Their duty was to account to the Federal Court, turn over the assets to the trustee and apply for and receive their compensation from the Bankruptcy Court for preserving the estate.

See also

Bryan v. *Bernheimer,* 181 U. S. 188;
In Re Williams, 240 Fed. 788.

In

Hume v. *Myers,* 242 Fed. 827,

the question was the same as was presented in *Silberberg* v. *Ray Chain Stores, supra.* The issue was between a Federal Court sitting in Equity and the Bankruptcy Court. The Court held:

"The true rule is this: When a Court of Equity appoints receivers of corporate property, its allowance to its receivers and their attorney is an administrative order, presumptively right as to the justice of the allowance. When the corporate property falls by operation of law into the bankruptcy court, that court by comity will indulge the presumption in favor of the correctness of the allowance;

but the court of bankruptcy having the responsibility of administration, must exercise its independent judgment, giving due weight to the presumption in favor of the administrative finding of the Court of Equity. This, we think, is what the Supreme Court meant in the case of In Re Watts, 190 U. S. 1, 23 Sup. Ct. 718, 47 L. ed. 933, when it said:

'It has been already assumed that the bankruptcy proceedings operated to suspend the further administration of the insolvent's estate in the state court, but it remained for the state court to transfer the assets, settle the accounts of its receiver, and close its connection with the matter. Errors, if any, committed in so doing, could be rectified in due course and in the designated way.'

The rectification of errors in due course and in the designated way here referred to must mean rectification by the bankruptcy court, for after the assets are turned over to that court all orders relating to the matter must emanate from that court."

See also *Quemahoning Creek Coal Co.,* 15 Fed. (2) 58. In the case of

In Re Rogers, 116 Fed. 435.

the Bankruptcy Court refused to recognize that the State Court had the power to transfer the assets to the bankruptcy receiver or trustee encumbered by a lien on the assets to insure the payment of fees to the state receiver. The Court held:

"There are, however, considerations involved in this question which are far graver than the loss of assets in a particular case. They involve the supremacy of the constitution and laws of the United States, the power of congress to create a uniform

> system of bankruptcy, the legislation creating that system, and the settled principle that insolvency proceedings in state courts are suspended while the bankrupt law is of force. *It is the duty of a court of the United States to take care that by no judicial order of its own the effectiveness and vigor of the laws with the enforcement and administration of which it is entrusted shall be nullified and whittled away.*"

This disposes of the contention of the petitioners (p. 11 of petitioners' brief) that the State Court officers had something in the nature of a lien on the assets.

The reason why the bankruptcy court is the only court that may fix fees after bankruptcy supervenes is apparent. If we leave the power to fix fees in the State Court that court may destroy the entire bankruptcy act since the amount of fees that may be awarded is discretionary with the Court. It may be argued that no State Court would allow the entire estate to its receiver. But by analogy we refer to the doctrine that the State Government may not tax an instrumentality of the Federal Government. The reason was stated in

> *McCulloch* v. *The State of Maryland* 4 Wheat. 579, 17 U. S. Sup. Ct. Rep. 316.

> "That the power to tax involves the power to destroy; that the power to destroy may defeat and render useless the power to create; that there is a plain repugnance, in conferring on one government a power to control the constitutional measures of another, which other with respect to those very measures, is declared to be supreme over that which exerts the control, are propositions not to be denied. But all inconsistencies are to be reconciled by the

magic of the word confidence. Taxation, it is said, does not necessarily and unavoidably destroy. To carry it to the excess of destruction would be an abuse, to presume which would banish that confidence which is essential to all government."

The power in the State Court to fix fees unrestrained by any Bankruptcy Court is the power to destroy the Bankruptcy Act created by the Act of Congress under the Constitution.

POINT V.

A State Court receiver is entitled to and will receive from the Bankruptcy Court just compensation and the repayment of his expenses for benefiting or preserving the bankrupt estate.

The difficulty in reconciling the State Court to a recognition of the paramount jurisdiction of the Federal Court lies in their fear that their receivers will not receive payment for their services in the Bankruptcy Court or as much compensation as they would have received from the State Court. With the latter question we have no concern, because the Bankruptcy Act provides a schedule of fees. But ever since *Randolph* v. *Scruggs*, 190 U. S. 533, 539, 23 Sup. Ct. 710 (47 L. ed. 1165), the Federal Courts have paid State Court receivers and assignees for their necessary work and labor in connection with the preservation of the estate.

See also

In re Chase, 124 Fed. 753 (1903);
In re Rogers (*supra*).

In the case at bar the Federal Court both invited and directed the Chancery receivers and their counsel to seek their compensation in the Bankruptcy Court (Record, pp. 13, 20 and 23).

Cases and Points Distinguished.

The following are some of the cases and points relied upon by petitioners in their brief:

Carling v. *Seymour Lumber Co.*, 113 Fed. 483, page 491 (Certiorari denied) 186 U. S. 484, 46 L. ed. 1261;

Ohio Motor Car Co. v. *Eiseman Magneto Co.*, 230 Fed. 370 (p. 16 of petitioners' brief).

These two cases merely relate how the paramount jurisdiction should be exercised. They suggest that the trustee should not make a peremptory demand on the State Court receiver, but should do it politely. In view of the conflict in New Jersey, a polite request by the Federal Court would have been denied. (See orders in Appendix B, where the State Court refused to surrender the assets, as occurred also in the case at bar.)

Loeser v. *Dallas*, 192 Fed. 909 (C. C. A. 3rd) (p. 63 of petitioners' brief),

where the Court said:

> "In the nature of this an ancillary receiver must be subject alone to, and obey the orders of, that court of which he is an officer. So obeying, it follows that to it alone must he account."

An examination of the case shows that the conflict was between a trustee in bankruptcy and an ancillary receiver in bankruptcy. It was a conflict between officials of courts of the same general jurisdiction under the bankruptcy act which recognized ancillary proceedings. It was not a struggle between courts of superior and inferior jurisdictions.

Mauran v. *Crown Carpet Lining Co.*, 23 R. I. 344, 50 Atl. 387;

Kennedy v. *American Tanning Co.*, 81 N. J. Eq. 109;

Shannon v. *Shepard Mfg. Co.*, 230 Mass. 224, 119 N. E. 768.

These cases seem clearly overruled by *May* v. *Henderson, supra, In re Diamond, supra. Re Williams, supra,* definitely disapproves *Mauran* v. *Crown Carpet Lining Co.*

Acme Harvester Co. v. *Beekman Lumber Co.*, 222 U. S. 300, 56 L. ed. 208.

This case rests either on estoppel or on the equitable doctrine of laches or on the specific finding of the Court that

> "The whole proceeding makes it clear that the district court *denied* the adjudication and declined to exercise its jurisdiction as a bankruptcy court."
>
> *Re Dayton Coal & Iron Co.*, 291 Fed. 390.

This case is relied upon extensively (pp. 16 to 18 of petitioners' brief) by the petitioners, and it will, therefore, be analyzed at length here. The essential question in the case was whether or not a decree made by a State

Court upholding the validity of a mortgage given by the corporation (later adjudicated bankrupt) was binding on the mortgagor's trustee in bankruptcy or, on the contrary, was subject to review by the Bankruptcy Court.

The Court held that the State Court's decree was binding on the trustee in bankruptcy and that the matter was not the subject of review by the bankruptcy court for the following reasons:

1. That the decree having been entered in the course of proceedings on "a general creditor's bill" was binding upon all general creditors of the mortgagor and was necessarily binding upon the trustee in bankruptcy as the representative of such creditors.

2. That the State Court decree in question was rendered "in the suit of an adverse claimant" to the (mortgaged) property and that that suit and the State Court's jurisdiction of the property involved therein were not affected by the bankruptcy proceedings because

> "The custody or constructive possession of the debtor's property which is vested in the bankruptcy court by the filing of the petition, *ex propria vigore*, extends, however, only to the property then held by or for him of which the Court might summarily take possession. * * * And it does not extend to property otherwise held as to which an adverse claimant has a substantial pre-existing claim of lien or title" (p. 396).

3. That the filing of a petition in bankruptcy "does not terminate the prior jurisdiction of a State Court in a suit to foreclose a mortgage."

Thereafter the Court proceeds "independently of the foregoing rules" to set forth views which are not necessary to a decision of the case, but on which they may rely. We shall therefore analyze them to show they do not apply. The Court says at page 398:

> "It is a general and fundamental rule of substantive law that a court which first acquires jurisdiction over property in controversy is entitled to retain that jurisdiction to the end of the litigation, without interference from any other court whatever, 3 Street's Fed. Eq. Pract., Sec. 2529, p. 1466."

As to this statement it is sufficient to say that the rule referred to is one which obtains only as between courts of *concurrent* jurisdiction and not as between courts of paramount and subordinate jurisdictions respectively, as where bankruptcy supervenes while a State Court receivership is pending. The Court next refers to certain language in the case of *In re Watts*, 190 U. S. 1, 23 S. Ct. 718, 47 L. ed. 933, wherein the Court seems to suggest that the said rule (which obtains between courts of *concurrent* jurisdiction) may have a "qualified application" where a State Court receivership is superseded by a bankruptcy proceeding, to the extent that such rule "still obtains as a rule of comity." As to this we beg leave to refer to pages 23, *et seq.* in our brief where we have fully discussed the *Watts* case and the language therein alluded to.

Next the Court refers to the case of

Eyster v. *Gaff*, 91 U. S. 524, 23 L. ed. 403,

as if that case held that a supervening bankruptcy had no effect upon the continuance of jurisdiction of a State Court whose receiver then had possession of the bankruptcy es-

tate. But that case lends no support whatsoever to that view. That case was an action in ejectment in which the plaintiff claimed title through a foreclosure of a mortgage. While the mortgage foreclosure suit was pending, a bankruptcy of the mortgagor supervened and the foreclosure decree was entered subsequently thereto. The defendant insisted "that all the proceedings in the foreclosure suit after the appointment of the assignee in bankruptcy are absolutely void, *because he was not made a defendant*" (See 23 L. ed. 404). The Court held that the State Court had jurisdiction to continue with the foreclosure proceeding after bankruptcy and to render a valid decree because "the debtor of a bankrupt or the *man who contests the right to real or personal property with him*, loses none of these rights by the bankruptcy of his adversary," and that although a (Federal) District Court which has adjudged a man bankrupt "draws to itself by that act * * *" *all control* of the bankrupt's *property* and *credits*, such bankruptcy does not draw into the Bankruptcy Court and out of other courts, litigation then pending in another Court relating to "*contested rights*" or "matters growing out of disputed rights of property or of contracts." In short, that decision was a vindication not of the jurisdiction of a State Court to control property of a bankrupt after supervening bankruptcy, but *the right of an adverse claimant* of property to continue to prosecute in a non-bankruptcy court his pending suit involving the *res*, despite the "bankruptcy of *his adversary.*"

The Court in the cited case next refers to the case of

Jones v. *Springer*, 226 U. S. 148, 33 Sup. Ct. 64, 57 L. ed. 161,

as if that case, too, lent support to the proposition that a bankruptcy proceeding does not terminate the jurisdiction of the State Court. In that case the suit was by a trustee in bankruptcy against an individual who had purchased property sold at judicial sale in a state court attachment proceeding, and the question before the United States Supreme Court was whether or not an order made by a state court in an attachment proceeding which ordered the attached property be sold "*on the ground that it was of a perishable nature and liable to be lost* * * * before the final adjudication of the case," was void and the sale made pursuant thereto invalid because, unbeknown to the State Court, a bankruptcy proceeding had supervened prior to the date of the said State Court order and sale. The Court held that it was not called upon to pass the question of the effect of the bankruptcy proceeding upon the jurisdiction of the State Court because "*whether it had jurisdiction or not* * * *" the State Court "had authority *from the necessity of the case* to preserve" the property in question "because the property was of *a perishable nature,*" the Court citing the language of Chief Justice Marshall to the effect that:

> "a right to order a sale is for the benefit of all parties, not because the case is depending in that particular court, but because the thing may perish while in its custody, and while neither party can enjoy its use" (see 57 L. ed. 164).

Next the Court (in the Dayton case) asserts that where bankruptcy has supervened, property in the hands of the State Court receiver "should not be taken from the receiver of the State Court by summary order or process of

the Bankruptcy Court, but in obedience to the rule of comity, application should be made to the State Court for an order directing its surrender," citing a large number of authorities in support of that statement. That proposition, we submit, may be conceded, but it is irrelevant. It means merely that the paramount bankruptcy jurisdiction should not be exercised brutally, but in a decent and orderly fashion by the making of an application to the State Court for an order directing its own receiver to surrender the assets *in recognition of the paramount bankruptcy jurisdiction.* Indeed, that proposition not only is consistent with the rule applied by the Court below in the case at bar, but acknowledges and presumes the existence of that rule.

Next the Court says:

> "In the light of the foregoing cases, I conclude that the prior jurisdiction acquired by a state court in a winding up proceeding, is not *ipso facto* superseded or suspended by the filing of a petition in bankruptcy, but that, as the state court cannot take judicial notice of the bankruptcy proceeding and is under the duty of proceeding in the case before it until informed of the changed relations of the defendant, it retains its jurisdiction in the winding up proceedings, under the rule of comity, until the pendency of the bankruptcy proceedings is brought to its notice and a request made to it by the bankruptcy court or a duly authorized officer thereof for the delivery of possession of the property of the defendant."

This conclusion, we respectfully submit, is not only unwarranted by the very authorities upon which the Court rests it, but is in itself untenable. It makes the question of the

State Court's continuance of jurisdiction after bankruptcy has supervened, depend on whether the State Court has been judicially informed of the bankruptcy proceeding or not, a proposition which, we submit, is a legal anomaly. If sound, it would mean that the paramount jurisdiction of the Bankruptcy Court attaches to property of the bankrupt in the hands of a State Court receiver *only if and when the State Court becomes judicially informed of the bankruptcy proceeding,* and it would make it possible for the Bankruptcy Act and the Bankruptcy Court's jurisdiction to be thwarted and defeated by a mere failure of interested parties judicially to apprise the State Court of the bankruptcy proceeding. We contend, however, that the efficacy and operation of the Bankruptcy Act does not rest on so precarious and casual a basis. The paramount jurisdiction of the Bankruptcy Court results from the filing of a bankruptcy petition and comes into existence in a given case the moment the petition is filed. See *Mueller* v. *Nugent, supra.* It does not await a communication of the bankruptcy proceeding to the State Court. It does not admit of a situation in which the jurisdiction of the Bankruptcy Court can be said to be a *jurisdiction in suspense.*

Immediately after making the statement last hereinabove quoted, the Court in the case under discussion goes on to say:

> "A contrary holding would, in my opinion be not only in conflict with the foregoing authorities and the rule of comity, but against a sound public policy. It would certainly lead to most disastrous results, to the wasting of the assets in fruitless litigation, and to great confusion, if, after the filing of the petition in bankruptcy the hand of the State court is to be deemed as stayed by the mere operation of law, so

> that when, without notice of the bankruptcy petition or any request of the bankruptcy court for the surrender of the assets, the State court proceeds in the due administration of the estate entrusted to its charge, adjudicating the rights of parties, selling and disposing of assets, and subsequently after an interval of months, or in case of contest and appeals, perhaps of years, an adjudication in bankruptcy is made, its jurisdiction is to be deemed to have been terminated, as matter of law, upon the filing of the petition and all its subsequent proceedings rendered thereby void."

As to this argument, grounded in an alleged public policy, we would remark:

1. In the case at bar the State Court receivers were notified in short order.

2. That it is not to be presumed that after a bankruptcy petition is filed, a State Court (in custody of the bankrupt's property) will, for any considerable time, remain in ignorance of that proceeding. Not only do all human probabilities and common sense expectancies preclude such a possibility, but the bankruptcy receiver, if one be appointed, would be under a duty immediately to take such steps as would be certain to acquaint the State Court with the fact of bankruptcy; or if no bankruptcy receiver were appointed the petitioners in bankruptcy or their attorney as well as interested creditors and other interested parties would be sure, in one way or another, to bring the matter to the attention of either the State Court or its receiver. If, however, such a remote possibility is to be entertained, it is an all-sufficient answer to say that the supremacy of the Fed-

eral law and the paramount jurisdiction of the Federal Courts thereunder can never be permitted to yield, if not in truth to abdicate, to an alleged "public policy" which is derived from so unlikely an abnormal and unrealistic an hypothesis as the one which the Court hereinabove postulates. If there is to be a choice between *upholding* the supremacy of the Federal constitution and laws and the paramountcy of the Federal Courts thereunder, at the risk of a remotely possible continuance of State Court administration in ignorance that its jurisdiction has lapsed because of bankruptcy, and the *overthrowing and abrogation* of the supremacy of the Federal constitution and laws thereunder in order to validate the post-jurisdictional action of a State Court, no one can doubt for a moment which alternative should and must be chosen. But secondly we would remark that if after supervening bankruptcy and in ignorance thereof, a State Court receiver were to sell and dispose of assets of the bankrupt estate, it does not follow that innocent third persons who dealt with the State Court receiver in good faith would be prejudiced by the rule which is applied in the case at bar. For, that rule, holding that the filing of a petition in bankruptcy terminates the jurisdiction and control of another Court over the bankrupt's property, does not necessarily operate to the prejudice or disadvantage of persons who have dealt with the receiver innocently and in good faith; for by analogy to Section 67-F of the Bankruptcy Law, it might still be held that with respect to such innocent third persons dealing with the receiver in good faith even after the filing of the bankrupt petition but in ignorance thereof, it might well and properly be held that their position and legal status would be regarded *as if* the State Court had had jurisdiction at the

time when their transaction or dealing with the State Court receiver took place.

However, we are prepared to argue that the rule in question is to be applied and the paramount Federal bankruptcy jurisdiction upheld even if it should operate to the prejudice and disadvantage of such third persons dealing with the State Court receiver *bona fide* and in ignorance of supervening bankruptcy; for even such persons are presumed to know that there is a Bankruptcy Law, that that law is constitutionally paramount, that bankruptcy may supervene at any time within four months after a State Court receivership, and that in dealing with a State Court receiver they are dealing with an officer of a Court whose jurisdiction and power is terminable and defeasible by a bankruptcy petition in the Federal Court. It may be argued that such persons deal with State Court receivers at their peril.

Finally and above all, it is incontestable that the Constitution and the laws thereunder must be upheld at all costs so long as those laws are in force, and it is the highest public policy to uphold those laws rather than defeat and thwart them. It is of the very nature of the dual system of government which obtains in our country that within the domain of Federal jurisdiction both the State Court and State government must subordinate and give way; and to say that State Court receiverships will be embarrassed or even defeated by upholding the Federal Bankruptcy Law is merely to state an inevitable consequence of the duality of our governmental system with its necessary incidents.

Our research shows that in *Re Dayton* has been cited in a number of cases but not in support of the proposition that

a State Court may fix fees after bankruptcy has supervened. These cases are:

Butler v. *Ellis*, 45 Fed. (2) 951 at page 954, (C. C. A. 4th), 1930;

Scott v. *Goodman*, 25 Fed. (2) 175 (1928), (recognizing *Lion Bonding Co.* v. *Karatz* as an authority);

Re Conservative Mortgage & Guaranty Co., 24 Fed. (2) 38 (C. C. A. 6th), 1928, (citing also in *Re Diamond, supra*);

Ft. Dearborn Trust & Savings Bank v. *Smalley*, 298 Fed. 45 (C. C. A. 8th), 1924:

Grand Rapids Dry Goods Co. v. *Ostendorf*, 6 Fed. (2) 506 (C. C. A. 6th), 1925;

(the payment to a creditor was made in this case after the petition in bankruptcy had been filed);

Iroquois Utilities, Inc., 297 Fed. 397 (C. C. A. 2nd), 1924;

(this case merely involved the foreclosure of a mortgage given more than four months prior to the filing of a petition in bankruptcy in which the District Court made an order directing the mortgaged property to be turned over to the trustee and enjoining the foreclosure suit. The Circuit Court reversed the order);

Re Nebraska Hotel Co., 1 Fed. (2) 24 (C. C. A. 8th), 1924;

(where Point 1 of syllabus reads: "After bankruptcy petition was filed, purchaser at sale by receiver appointed by state court, which, with proceedings on which it was

based, were declared void by state Supreme Court, was not adverse claimant; state court having at no time acquired jurisdiction of *res.*") (This case is not in support of the claims of the petitioners herein).

In the petitioners' brief it is argued that the rights of a receiver in New Jersey are greater than that of an assignee; that not only has he possession but also title (page 25 of petitioners' brief); that the proceedings under the New Jersey Statute are in the nature of an equitable *quo warranto* (page 55 of petitioners' brief); that the receiver is an independent ego (page 56 of petitioners' brief); that the receiver is the corporation plus (page 57 of petitioners' brief), and that the receiver therefore is on a higher plane than a mere assignee who takes by the voluntary act of the parties.

It is true that the proceedings in New Jersey have been likened to an equitable *quo warranto* proceeding. As was pointed out by Vice-Chancellor Stevenson, the main object of the bill of complaint is not the appointment of the receiver, but the passing of an injunction to enjoin the corporation from exercising its privileges and franchises. Unless the Court grants the statutory injunction there is no jurisdiction to appoint the receiver as incidental relief. The granting of an injunction is an absolute condition precedent to the appointment of a receiver. See

Gallagher v. *Asphalt Co. of America*, 65 N. J. Eq. 258.

Since it is a suit against the corporation itself, how can the Court justify the injunction orders described in Appendix B against persons not parties to the suit?

That the receiver is not the corporation plus is manifest from the trend of recent decisions of the Court of Errors and Appeals, the Court of last resort in all causes in New Jersey. In the administration of the estate the receiver may become aggrieved at a decision of the Court of Chancery of New Jersey affecting the corporation's assets. If he is the corporation sole or the corporation plus or an independent ego, he should be permitted to appeal to the Court of Errors and Appeals as a matter of right because his property rights have been affected by the adverse decree. The Court has held, however, that the receiver may not appeal as of right but may do so only with the permission of the Court that appointed him.

Crown v. *Regna Construction Co.*, 106 N. J. Eq. 192 (Errors and Appeals 1930);
Mortgage Security Corp. of N. J. v. *Townsend*, 108 N. J. Eq. 268 (Errors and Appeals, 1931);
Seidler v. *Branford Restaurant*, 97 N. J. Eq. 531 (Errors and Appeals 1925) as to the status of a receiver.

This court has extended the law relating to assignees to receivers. *Stellwagen* v. *Clum, supra.*

In

Bankshares Corporation of the United States, 50 Fed. (2) 94 (C. C. A. 2nd) 1931,

the contentions of petitioner with respect to the status of a New Jersey receiver as to his title were fully considered and determined adversely to the contentions of the petitioner.

The Circuit Court of Appeals held as follows in disposing of this contention:

> "The New Jersey receiver as such has no standing to intervene in the District Court for the Southern District of New York. Moore *v.* Mitchell, 281 U. S. 18, 50 S. Ct. 175, 74 L. Ed. 673; Burrowes *v.* Goodman (C. C. A. 2), 50 Fed. (2) 92, decided May 18th, 1931. The injunction issued against the board of directors by the New Jersey Chancery Court does not extend beyond the jurisdiction of that court. The corporation had its principal place of business within the Southern District of New York, and the directors met there and passed a resolution authorizing its attorney to consent to the adjudication in bankruptcy. See Bonnifeld *v.* Thorp (D. C. Alaska), 71 F. 924. The Bankruptcy Act is paramount. In re Watts & Sachs, 190 U. S. 1, 23 S. Ct. 718, 47 L. Ed. 933. The New Jersey act is not in conflict with the provisions of the Bankruptcy Act. There is no provision of the Bankruptcy Act which exempts a New Jersey corporation from an adjudication thereunder merely because of insolvency proceedings resulting in a receivership, pending in the state of its creation. No state enactment may limit the jurisdiction of the bankruptcy court. International Shoe Co. *v.* Pinkus, 278 U. S. 261, 49 S. Ct. 108, 73 L. Ed. 318."
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> * * * * * *
>
> "In Struthers Furnace Co. *v.* Grant, 30 F. (2) 576 (C. C. A. 6), the state court receiver sought to intervene for the purpose of vacating an adjudication in bankruptcy, and advanced the claim that the corporation had consented in the state receivership to bar itself from entering into a voluntary bankruptcy petition under section 4a of the Bankruptcy Act, 11 U. S. C. A. Section 22 (a). But this contention was overruled. In that case, the Ohio state

> statute for the appointment of a state receiver vested all the property of the corporation with such receiver, and the receiver was no mere custodian, but had full power to act for the corporation. Throckmorton's Ohio Code (1926), Section 11945, Rev. St. Section 5658; section 11897, Rev. St. 5590. A bankruptcy petition will supplant a state court receiver on application therefor. In re Dressler Producing Corp. 262 F. 257 (C. C. A. 2). The authorities appellant relies on, referred to above, are not inconsistent with these views."

See also

In Yaryan Naval Stores Co., 214 Fed. 563 (C. C. A. 6th, 1914).

It is argued by petitioners "that the New Jersey Corporation Act so far as its insolvency features are concerned is not suspended by the Bankruptcy Act" (page 51 of petitioners' brief).

The New Jersey Courts however, have uniformly held that the statute in question is essentially a Bankrupt Act.

In Bloch v. *Bell Furniture Co.*, 111 N. J. Eq. 551, 162 Atl. 414 (1932),

the Court held:

> "The essentially bankrupt character of our statute concerning insolvent corporations was recognized by this court in Butler *v* Commonwealth Tobacco Co., 74 N. J. Eq. 423, 70 Atl. 319. The practical advantage of maintaining a harmonious doctrine in the administration of the assets of an insolvent corporation in the State and Federal Courts, where the provisions of our statute and the rationale of our jurisprudence permit, is apparent. Nutz

> *v.* Murray-Nutz, 109 N. J. Eq. 95, 156 Atl. 668. For one thing, it tends to avert an unseemly race for jurisdiction in the interest of one or another class of creditors. Napier *v.* People Stores Co., 98 Conn. 414, 120 Atl. 295, 33 A. L. R. 499."

In the Bloch case the New Jersey Court of Errors and Appeals adopted the bankruptcy rule as to the provability of claims for anticipatory breach of lease. Since it is a bankrupt act *it must follow that when bankruptcy supervenes the New Jersey Corporation Act insofar as the insolvency phases are concerned is immediately suspended.*

POINT VI.

The order of the District Court as affirmed by the Circuit Court of Appeals should be affirmed in all three cases.

Respectfully submitted,

SAMUEL KAUFMAN,
Of Counsel with Respondent.

SAMUEL KAUFMAN,
NATHAN BILDER and
ARTHUR LEONARD ROSS,
of the New York Bar,
Of Counsel.

Appendix A.

Section 65 of the Corporation Act, under which State Court receivers are appointed, reads as follows:

> "Whenever any corporation shall become insolvent or shall suspend its ordinary business for want of funds to carry on the same, or if its business has been and is being conducted at a great loss and greatly prejudicial to the interest of its creditors or stockholders, any creditor or stockholder, or stockholders, *provided* such stockholder or stockholders own at least ten percentum of the capital stock of such corporation, may by petition or bill of complaint setting forth the facts and circumstances of the case, apply to the Court of Chancery for a writ of injunction and the appointment of a receiver or receivers or trustee or trustees, and the court being satisfied by affidavit or otherwise of the sufficiency of said application, and of the truth of the allegations contained in the petition or bill, and upon such notice, if any, as the court by order may direct, may proceed in a summary way to hear the affidavits, proofs and allegations which may be offered on behalf of the parties, and if upon such inquiry it shall appear to the court that the corporation has become insolvent and is not about to resume its business in a short time thereafter, or that its business has been and is being conducted at a great loss and greatly prejudicial to the interest of its creditors or stockholders, so that its business cannot be conducted with safety to the public and advantage to the stockholders, it may issue an injunction to restrain the corporation and its officers and agents from exercising any of its privileges or franchises and from collecting or receiving any debts or paying out, sell-

ing, assigning or transferring any of its estate, moneys, funds, lands, tenements or effects, except to a receiver appointed by the court, until the court shall otherwise order. (L. 1896, ch. 185, p. 298, Section 65 (C. S., p. 1640, Section 65), as amended by L. 1912, ch. 300, p. 535, Section 1; S. 47-65; as amended by L. 1931, ch. 221, p. 545.)"

Appendix B.

Types of injunction orders issued by the New Jersey Court of Chancery as described in the brief and all on file in the Docket in the office of the Clerk of the Court of Chancery of New Jersey.

(1) *Albert & Kernahan* v. *Monitor Park Theatre Co.*, Docket 70, page 352:

"That all persons stockholders of the defendant and firms or corporations including sheriffs and marshals and their officers, agents, attorneys, representatives, servants and employees, whether creditors or claiming to be creditors or having or claiming to have any right, title or interest of, in and to any property or properties of the defendant corporation, be and they hereby are enjoined and restrained from instituting or prosecuting or continuing the prosecution of any action instituted under and by virtue of the United States Bankruptcy Act, and the various amendments thereof and supplements thereto, without first giving the receiver herein appointed at least five days' notice of the institution, prosecution or continuing the prosecution of any such action, and at the same time serving upon the

said receiver copies of petitions, affidavits, orders and other pleadings intended to be presented or used thereon."

For a similar order see

C. F. Albert Lumber Co. v. *Kenvil Lumber & Store Co.*, Docket 76, page 16.

(2) *Tappen & Indruck Co., et al.* v. *Delpark, Inc.*, Docket 85, page 470:

"And it is further ORDERED that the said corporation, its officers, servants and agents are hereby restrained and enjoined from taking any corporate action for the purpose of having a receiver appointed for the defendant company in any other cause."

NOTE: (It is interesting to note that the defendant was a New York corporation. This order enjoined the corporation from exercising the privileges and franchise granted by the State of New York.) Compare *Rogers* v. *Guaranty Trust Co.*, 53 Sup. Ct. Rep. 295.

A petition in bankruptcy was filed in New York. The company consented to an adjudication and no contempt proceedings were brought in New York against the New York directors. In

(3) *Frank C. Zuch* v. *Atlas Fence Company*, Docket 95, page 226,

the order read as follows:

"AND IT IS FURTHER ORDERED, that until the further Order of this Court, all and singular the creditors and stockholders of said corporation, and all other persons whatsoever, be and they hereby are restrained from instituting, prosecuting or proceeding with any action in any court or tribunal whatsoever at law, in equity or in bankruptcy."

In

(4) *Benjamin* v. *Up-to-date Laundry Service, Inc.*, Docket 88, page 25,

the order read as follows:

"That the receiver herein until such time as the further order of this Court, retain in his possession all of the assets of said alleged bankrupt and do not surrender said assets to any trustee or receiver appointed in any Court of bankruptcy or to any officer of any other court or any person whomsoever without first having presented his report and account to this Court and having his account passed by this Court and his compensation fixed, the said receiver being authorized to retain said assets in his own right as an adverse claimant and in the right of this Court."

NOTE: (In this case the Court of Chancery ordered the assets sold after adjudication in bankruptcy; the receiver sold and delivered a bill of sale to his vendee.)

(5) *In the Matter of the alleged contempt of Frederick C. Henn, Spencer D. Baldwin and John M. Struble,* Docket 94, page 284,

the order read as follows:

"ORDERED, that Frederick C. Henn, Spencer D. Baldwin and John M. Struble show cause before the Chancellor at Chancery Chambers at 1060 Broad St., Newark, New Jersey, on the 7th day of January, 1933, at ten o'clock in the forenoon or as soon thereafter as the matter can be heard, why they should not be adjudged guilty of contempt of this court in the premises and punished accordingly."

NOTE: (In this case the contempt charged was a criminal contempt.)

For a similar order see

Muller v. *Mt. Holly Textile Co., Inc.*, Docket 94, page 691.

(In this case the contempt charged was a civil contempt.)